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Mills, A.L.

The duties of a banker

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*The
Duties of a Banker*

ADDRESS DELIVERED BY

A. L. MILLS

President First National Bank, Portland, Oregon.

AT THE

WASHINGTON STATE BANKERS CONVENTION

HELD AT

WHATCOM, WASHINGTON

JULY 23, 1903.

The Duties of a Banker

Mr. President and Gentlemen:

Were I called upon to name in their order the chief duties of a banker I should say:

First: To safeguard the funds entrusted to his care.

Second: To facilitate the commerce of the community.

Third: To earn adequate dividends for his stockholders.

Fourth: To act as a conservative element in the community and to aid in moulding public opinion.

When a bank receives deposits it agrees to return them on demand, unless some specific contract to the contrary is entered into. The only pact with the ordinary depositor is to return his money when demanded; a failure so to do means the failure of the bank. Nevertheless for a bank to have on hand at all times the funds necessary to pay every depositor in full would destroy many of the useful functions of the bank and would convert it into a safe deposit vault. How then can a bank be so conducted that it can be reasonably sure of fulfilling its obligations to its depositors?

The merest tyro at banking or the most crassly ignorant of depositors knows that time and experience have demonstrated that a reasonable amount of a bank's deposits may be utilized to perform the other duties of a bank. What then is a reasonable amount to so utilize, or conversely, what proportion of a bank's liabilities should be kept in cash, in reserve, and what disposition should be made of the remainder in order that a banker in addition to his other duties may be reasonably sure of fulfilling his duty to his depositors?

No hard and fast rule can be laid down, applicable at all times and under all conditions; at best we can but approximate. There are times when a banker can meet his deposit-

ors smilingly with but a ten per cent. reserve and there are other times when his mind is tortured at the thought that he has not coin in his vault to cover every dollar of his deposits. A banker cannot be a coward; he is ever sleeping on a magazine that at any time may explode and wreck his institution; let but an ugly rumor concerning the bank's solvency get started, it will spread like fire in dry prairie grass, and the mischief is done. The banker is ever using without law or license, largely for the profit of his stockholders, the funds entrusted to him for safe keeping; custom may sanction such use, but the law does not grant it.

What is reasonably safe banking in one section of the country is not in another, and what may be good banking in New York, for instance, may be poor banking on the Pacific Coast. To illustrate: In May, 1893, I asked Mr. Perkins, late President of the Importers & Traders National Bank, if, in case the Security Savings and Trust Company should be in need of funds the coming summer, could his institution grant us an accommodation on the pledge of our Government and railroad bonds?

"You may have what you want now, Mr. Mills, but what are you doing with those bonds? It is not good banking to invest your money in railroad securities." I replied that we held them in order to have an anchor to windward, in order to have some quick assets in just such times as appeared near at hand.

"But you are wrong, Mr. Mills, you have a false idea of how to prepare for financial storms. Do as we do when we see our reserve running low; call in your demand loans; if that does not suffice and the drain continues, take your tickler and give instructions to collect your maturing paper."

I answered that banking in New York and in Portland, Oregon, were two entirely different propositions, and principles that would apply in New York were not applicable to the Coast; that if a panic struck Portland we could call our demand loans until we were hoarse without avail and that

to force collection of maturing paper would be a confession of weakness that would act as a boomerang on the bank.

And Mr. Perkins' comment was: "Then if such is the case in Portland, I would have nothing to do with banking and I should advise you to seek some other occupation."

No exact rules and regulations can be laid down to govern banking alike in all parts of our country. The National Bank Act attempts to do so but its cast iron provisions are often honored in the breach. The Act states for instance, that a National Bank shall not loan on real estate mortgages, and the restriction may be a good one for banks in our large cities, but what country banker does not know that in our farming communities no better security can be obtained for a portion of his funds than land?

But I have wandered somewhat from the point at issue: What in our Northwest is a reasonable reserve, and what is a reasonably safe use of the balance of the bank's funds, bearing in mind always that a banker's first duty is to his depositors?

Mr. Horace White in his account of the Suffolk Bank System writes as follows: "It was not until 1858 that the State of Massachusetts in consequence of the panic of 1857, established a legal reserve of 15 per cent. of specie against both deposits and circulation. . . . Prior to the passage of the law of 1858, the specie reserve had been extremely variable, ranging from 44 per cent. in 1843 to 7½ per cent. in 1851. . . . This law did not touch the other New England States, whose banks were integral parts of the Suffolk System. In 1859, Maine, Rhode Island and Connecticut each had 10 per cent. of specie as against circulation and deposits, New Hampshire 7½ per cent. and Vermont only 6 per cent.

Under the present National Bank Act, in other than reserve cities, a bank is permitted to loan all but 15 per cent. of its liabilities; of this 15 per cent. three-fifths may be deposited in a reserve city; and the banks of a reserve

city are permitted to deposit one-half of their 25 per cent. reserve in New York, Chicago or St. Louis, where the National Banks are required to keep but 25 per cent. in coin. Has it ever occurred to you how small an amount of coin is 'hus behind the deposits of the country? How dependent all the banks of the country are upon the resources of the great banks of New York, Chicago and St. Louis? The restrictions of the National Bank Act may, in the opinion of the framers of that law, be sufficient protection to the depositors but does anyone here think it reasonably safe banking to have but a little over 6 per cent. in cash behind his deposits? And yet a compliance with the National Bank Act requires but that much coin. For instance, a National Bank in Whatcom has \$400,000 deposits; of its \$60,000 reserve \$36,000 may be kept in Portland; against the \$36,000 Portland must keep a reserve of \$9,000 of which \$4,500 may be in New York, and New York is required to keep but \$1,125 of this on hand. To meet the \$400,000 in Whatcom the requirements of the National Bank Act are fulfilled with only \$29,625 cash, or a trifle over 7 per cent. This may be sufficient protection to the public, but when Uncle Sam deposits his money, he requires as security dollar for dollar in his own obligations. When we note how closely the banks of the country are knit together, how dependent they are upon one another, is it a matter of wonder that a panic in Wall Street is felt throughout the length and breadth of the land? Is it wise to be so dependent? Should our banks not be more independent? And to do so should they not carry more of their reserve in their vaults and in near-by cities?

Is the 15 per cent. rule of the National Bank Act a safe guide? Consider the difficulty, nay impossibility of collecting our loans in times of panic; consider that our people will be satisfied with nothing short of gold coin when panic drives them to the bank doors; that we cannot issue Clearing House Certificates that pass current for the coin

of the country, practically suspending specie payments as New York did in '93. Consider these facts and ask yourselves if a 15 per cent. reserve is sufficient preparation for the evil days that are sure to return? The pendulum of prosperity swings backwards and forwards, has it almost reached the limit of good times?

To conduct a bank on a 15 per cent. reserve and in troublous times to depend upon larger institutions for loans or rediscounts is most dangerous. In fact when a panic strikes the country the larger banks are apt to call in their loans made to correspondents; self-preservation becomes the first law; every bank for itself and the receiver take the hindmost. With the conditions prevailing here, it is the bankers duty to carry in his vaults a large amount of cash and his larger balances should be near at hand. In '93 it was extremely difficult to make collections on the banks in the East and the transfer of coin to this Coast was accomplished at heavy cost and with much difficulty. At that time we had a draft for a considerable amount on a solvent Philadelphia Bank. Our New York correspondent sent it back with the comment "Cannot collect on Philadelphia." We returned it with instructions to present again, hold, and wire fate. Our correspondent wired, "bank will honor only in Philadelphia exchange we cannot credit your account." We answered "send collection by special messenger, demand coin or close the bank." The above story is from memory, but the history of the collection is practically as I have given it. The collection was paid, but we lost many valuable days and paid a heavy exchange charge.

As I have remarked previously, no hard and fast rule, applicable to all conditions, can be laid down for the amount of reserve a bank should carry, but I believe, and in the light of past and existing laws, I venture the advice with much diffidence, that a bank in the Northwest can feel only reasonably safe with a reserve at all times of 25 per cent. of its demand liabilities (15 per cent, of which at least

should be in its vault) and in addition 25 per cent. of its loans should be good, quick convertible Wall Street securities.

Mr. Horace White says "it is desirable that a bank should have a portion of its interest-bearing assets so invested that it can be quickly turned into cash to meet emergency. This is specially needful in the case of a bank which holds large sums deposited by other banks, since a financial disturbance occurring in a distant quarter may bring sudden demands for cash from these depositing banks. Stock Exchange securities are held by banks partly because they can be sold at short notice to meet such emergencies, etc."

Should one however share Mr. Perkins' objections to bonds, then the bank should keep a 50 per cent. reserve. A fifty per cent. reserve seems large and not especially apt to gladden the heart of a stockholder, but I spoke advisedly when I said it was only reasonably safe. In a neighboring city, I am told, a bank went into the panic of '93 with that reserve; its Directors viewed the troubles with complacency; they made no attempt to strengthen their position; on the contrary, their cupidity urged them to take new business and their neighbors unloaded on them; before they knew it the bank was in deep water; it was too late to obtain aid and soon those ugly rumors were afloat that start no one knows where; the bank was obliged to close its doors and the receiver performed the last sad rites.

Much more could be said of a banker's duty to his depositors, but in some lame fashion I have tried to set forth what I believe to be his duty in this respect concurrent with his other duties.

To facilitate the commerce of a community, I have called the banker's second duty.

Ricardo has said "the distinctive function of a banker begins when he uses the money of others." If a bank acts simply as a storehouse for the funds of its depositors, it becomes a safe deposit vault; it ceases to perform one of its

chief duties and instead locks up the funds of a community that should be used to aid the wheels of commerce.

The necessities of commerce called banks into being. At first their functions were simple; the great banks of Italy and Holland were mediums of exchange for the clipped and mutilated coins of other countries. In early days interest was a crime; interest and usury were synonymous terms. Gradually the usefulness of banks became apparent and their functions extended. Prejudice disappeared and today it is the interest account that in most cases supports a bank. It was said years ago that no European power dare undertake war without first consulting the Rothschilds; possibly today it is Mr. Morgan. Hamilton recognized the functions of a bank when he planned the financial framework of our country and the removal of the public deposits in the thirties shook the country to its foundations.

As a pond is formed by many little streams and springs and the overflow is used to turn the wheels of a mill, so a bank gathers size and strength from the thousands of small depositors and the surplus is, and should be, used to turn the wheels of commerce. Recognizing this duty, to whom and to what extent should the funds of a bank be loaned?

Those borrowers who have first claim on the funds of a bank are its depositors, those who have shown their faith in the institution, and the measure of the claim should be the value of the account.

Next are those well established industries that go to make up the life of a community, the great lumber, wool, wheat, salmon and manufacturing interests, the great wholesale and retail houses, by whose efforts and enterprise our cities prosper.

Finally come the miscellaneous loans that are taken simply to swell the earnings of a bank, such as warrants of distant cities and countries, loans to interior merchants and commercial paper purchased in Eastern cities simply for investment.

Let us consider the first class mentioned, those borrowers who are depositors in the bank; to what extent should they be accommodated? The National Bank Act limits a loan to 10 per cent. of the bank's capital, but the rule is often broken, else how could a bank like the Chemical National in New York do business on a \$300,000 capital and \$7,000,000 surplus with a limit on its loans of \$30,000? An officer of a New York bank not long since said to me "our excess loans are our best ones and Mr. Dawes acknowledged he had usually found it to be the case."

Nevertheless the 10 per cent. limitation is good, and useful at times, especially to stand off importunate borrowers; but without injuring its efficiency, it might be stretched to include 10 per cent. of a bank's capital, surplus and undivided profits; especially might this be were the borrower a depositor, since in this case a bank usually has a portion of its loan on deposit. In some Eastern cities a customer is required, or at least expected, to keep on deposit a quarter of what he borrows, thus reducing the amount a bank has at risk.

This leads me to speak of another point of difference between the East and our Coast, somewhat irrelevant I confess, but one with which we have all been confronted. How often have you been asked why you demanded such a high rate of interest when the New York banks were loaning at so much lower rate? Of course the law of supply and demand governs largely but the slack principles we follow are partially to blame. Do we ever expect a demand loan to be paid on demand? Do we really anticipate a ninety day loan will be paid at maturity? Do we refuse a partial payment at any time or refuse to allow a credit for interest by virtue of such payment? In fact are we not apt to call a customer "prompt pay" who, without a thought of the principal (unless he has been severely reminded) steps up to the counter and pays his interest only on the maturity of his note? I have even known borrowers to complain about

paying interest accrued after the maturity of a note because they had failed to receive a dun. It is this looseness on our part, this failure to educate the public to the duty they owe the bank, that makes banking in the Northwest difficult; and it is from not understanding our loose methods that Mr. Perkins exclaimed that we did not know the principles of good banking. Were our merchants made to understand the nature of their obligations; that, unless previous arrangements were made, the note must be met at maturity, that partial payments would not receive consideration in the computation of interest, that the extent of their right to borrow would be measured by the size of their daily balance, the disparity of rates of interest between the East and the West would not be great and our banks could figure with some slight degree of certainty upon the availability of their assets in the note pouch.

Then again another difference between banking in the East and West. In New York there is such a thing as a money market and rates of interest fluctuate with the supply and demand. There a bank's funds earn proper return when the money market is tight. How is it with us? Does the rate respond to the condition of the local money market? Is it not that our rate is constant and that loans are refused as the supply of funds diminishes? As times have grown better and money become more plentiful in the Northwest our ruling rate has steadily fallen, but does it ever rise with a stringency? What results? When times are good and money easy everywhere our best customers seek the lower rates of New York; when times are bad and money tight everywhere they come home to be cared for by their local banks. No one blames them, it is simply common sense to pay as little as possible for money, but it helps to complicate the management of a Western bank. However until we grow stronger and more independent and govern our business according to prevailing conditions, the situation will remain unchanged.

I have said that next to a bank's depositors the commercial enterprises of a community have a claim on the funds of a bank.

Few banks, single handed, can carry some of the large enterprises of a community; because such an enterprise does not keep an account it should not be refused accommodation and the bank's funds loaned in the East. Its funds have been deposited by the community and in a measure it is a breach of trust to deprive the home community of the benefit of them. But in loaning to other than his depositors, a banker must exercise great care; he must consider well the reasons for the application; it may be but the kindly effort of a fellow banker to unload an undesirable account; if collateral is offered, the kind of collateral must be scrutinized. It has been thought that warehouse receipts for grain were the best of collateral, but note the Eppinger failure in San Francisco. It is safe to value warehouse receipts but lightly when the warehouse is owned or operated by the borrower; a criminal suit is but small compensation for lost money. An interior warehouseman often has slight conception of the difference between meum and teum and the banker may wake to find that warehouse receipts like fiat money have nothing behind them.

A banker is often tempted to loan too freely to those enterprises in which either he or his directors are interested. If you analyze bank failures you generally find such loans to be one of the chief causes. One from whose advice and counsel I gained much in the past, Mr. Henry Failing, once said to me: "When in doubt about the propriety of making a loan I say to myself 'whose money are you loaning' and the thought it was not my own but funds intrusted to me for safe keeping, has saved the bank from many a loss." Another remark of his was "a banker can not afford to have friends." How many of us in a moment of weakness have loaned against our instinct money to some "good fellow" and later have mournfully placed the obligation in that col-

lection of thumb worn relics marked "charged to Profit and Loss?"

It is hardly necessary to speak of loans where an interest in the enterprise is offered as additional inducement, yet I have heard of institutions, where unless the banker was let in on the ground floor, one could not get a loan. Such a false conception of a banker's duty is unworthy of more than mere mention.

The third duty of a banker, as I have classed his duties, is that of earning dividends for the stockholders.

To earn dividends for the stockholders certainly is one of the chief duties of a banker, since without the prospect of adequate returns on the capital invested few banks would be organized; nevertheless the desire to fulfill that duty to the entire satisfaction of all the stockholders, exposes a banker to the gravest dangers.

Often the success of a bank is measured by the size of its dividends and the success of the bank often is the gauge of the qualifications of the manager. Yet many a bank that pays but small dividends performs most useful functions in the community; better 6 per cent. dividends with all other duties fulfilled than 25 per cent. dividends with every available dollar loaned out at the highest rate obtainable. The devil, standing behind every manager's chair, urging him to take this or that piece of risky business, to let his reserve run low, or to take chances on the future for the sake of the present, tempts him with the plaudits of his stockholders and the consequent appreciation of his services. It is hard to conduct a bank safely and withstand the temptation of risky business at high rates when one's stockholders complain of small dividends.

It may be that I have spoken in a slighting manner of a bank's stockholders and given the impression that their only thought was the size of their dividends. This is true of many but there are others, and the majority I hope, who appreciate the higher duties of a bank and who are proud to

be part owners of an institution that is known to be sound to the core.

It might be inferred also that a banker performed his duty to his stockholders best when he paid them the highest dividends. This is not altogether true. His duty is best fulfilled when the bank is so conducted as to be a source of pride to them and the community; when its credit, like the Rock of Gibraltar, is impregnable; when, be the dividends what they may, the bank performs its other functions faithfully, honestly and conscientiously.

To act as a conservative element in the community and to aid in forming public opinion I have called the final duty of a banker.

No one can deny the great influence exerted in the community by the managers of its financial institutions. By the very nature of their calling they inspire confidence and their words are listened to with respect and consideration. Into their ears are poured the business secrets of a community and their opinions are spread widecast abroad. How carefully then must their utterances be guarded! Their calling demands conservatism; your optimist is generally a wildcat banker and your pessimist is usually the safest banker to whom to intrust your funds. Let the bankers foster every boom proposition in a city and how long before its citizens are in sack cloth and ashes! Let others do the booming and let the bankers preach conservatism.

The bankers of a community are in its every council, members of its clubs, committees, and trade organizations; upon them more than upon any other class of its citizens rests the duty of moulding public opinion. Do we fully appreciate this responsibility? Are we careful enough of our words when we think how far they carry? Recently it was said of Mr. Williams, late President of the Chemical National Bank, that "in times of inflation he was conservative and safe; in times of financial stress, calm and strong; he was the best type of the high minded commercial banker."

Can we feel in any small measure, each of us, that such words of praise can be uttered of our endeavors?

One more word in this connection, applicable to our local conditions in the Northwest.

We all know well the jealousies of our leading cities. How contemptuously they refer to Spokane as a windbag harnessed to a waterfall; how Seattle is jeered at as famous for nothing but its padded clearings and its criminal element; how Tacoma is said to be commercially dead and living only on its past glory; how Portland is a back number in the last stages of decomposition on the muddy banks of a ditch!

Now, my friends, do we who are supposed to be of so much weight in our local communities, encourage this spirit or do we stand on a higher plane than the liars and the carpers?

President Roosevelt remarked: "It can not be said too often that it is never detrimental to any section of the country to have another section built up." Do we preach this doctrine?

Do we give due praise to the men of Spokane who, undaunted by disaster, reared their city again from its ashes and whose spirit and enterprise have harnessed that mighty waterfall so that today its force is felt in the mines of Coeur d'Alene, fifty miles away?

Do we accord to Seattle the admiration it deserves? Blasted by fire, sidetracked by the great railroads, the indomitable spirit of its people reared a greater, nobler city on the site of the old and compelled the railroads to come suppliant to Seattle's doors.

And Tacoma, founded, fostered and aided by a great corporation, when that corporation in great measure withdrew its support, did not Tacoma's people manfully take up their burden and make of their city one of the most beautiful and active business centers of our Northwest?

And of Portland, my own city, do you of Washington

often say a good word? Is Portland dead, is it lacking in enterprise? In three days we raised \$350,000 to exploit to the world the resources of our great Northwest. From our own pockets we have expended over \$1,300,000 to dredge out our river with never a whine to Congress for help, and within a year by our own resources have we opened to rail connection one of your beautiful valleys, the Klickitat, at a cost of nearly a million dollars.

But enough, the subject is one on which I could easily dilate at length but the point is made if I have brought to your minds one of our great duties, namely, to aid in forming a proper public spirit in our own communities, a spirit of generous rivalry, a spirit of emulation not of envy.

Let us go back to our duties with a higher conception of them if possible; let us teach and practice that in unity is strength; that our great Northwest is one country and destined to be the greatest of these United States; that there is room for all and many more; that to build up is better than to tear down; that only by all working together for the good of all can we attain that growth and that position to which by all the blessings of soil and climate and geographical position we are justly entitled.

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